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How South Korea Could Win, and Lose, in Trump's Tech War

The U.S. Huawei ban could provide a boost to South Korean competitors, but will bring long-term costs as well.

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The decision by the United States to place Chinese telecoms giant Huawei and its affiliates on the “**Entity List**” effectively bans U.S. telecommunication firms from continuing to service and supply Huawei products. Over the next few months the decision will limit or cut off Huawei’s access to critical U.S. parts and software that it needs to maintain its growth potential outside of China, essentially **expanding the U.S.-China trade** war into a tech war to determine who will build the infrastructure for 5G technologies.

Few countries are perhaps as well placed to take advantage of the Huawei ban as South Korea. One of the world’s **leading tech economies**, South Korea ranks among the **top five** countries in the world in high-tech exports. It’s also specifically well placed to provide the smartphones and networking equipment that Huawei may now face challenges selling abroad.

The ban could also come at an opportune time for South Korea. Slowing **domestic demand** and decreasing exports saw first quarter GDP **decline by 0.4 percent**, while the trade war between the United States and China may be beginning to take a toll. Exports to China for the year-to-date are **down 14.1 percent** and increased exports to the United States have not made up the difference. Increased tech exports could help boost the economy.

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Among South Korean companies, many **commentators see an opportunity for Samsung specifically to benefit from U.S. efforts to blacklist Huawei**. How much Samsung could gain in areas such as smartphones, however, will depend on how long U.S. companies are **banned from working with Huawei**.

As the leading producer of smartphones, Samsung competes directly with Huawei in the high-end and mid-price model ranges. Prior to the ban, Huawei had targeted 2020 to **unseat Samsung** as the world’s top selling smartphone brand. Without access to Google’s Android and Google apps, along with chip designs provided by ARM, Huawei could find it difficult to compete with Samsung outside of China.

Not only will the prospect of Huawei surpassing Samsung in smartphone sales be pushed back, but **one estimate** suggests that if Samsung were able to capture half of Huawei’s market share outside of China, it could earn an additional \$1.13 billion in operating profit. That would be equal to about 14.1 percent of the operating profit of Samsung’s mobile division.

The ban could also help Samsung in the **foldable phone space**. When Samsung developed its first phablet with the Galaxy Note, the phone created a new market space where Samsung was able to profit until Apple moved to make larger phones as well. The foldable phone could be a similar area where Samsung benefits from being a first mover, but the launch earlier this year faced problems and, unlike with the Galaxy Note, Huawei was set to challenge Samsung in the foldable space with the Mate X at an early stage. If Huawei is no longer able to use Android as the Mate X's operating system, it could create an opportunity for Samsung to overcome the **launch problems**.

Huawei's difficulties could be especially beneficial to Samsung's networking business. During the 4G LTE wireless phase, Samsung's networking business was unable to secure any major clients for its equipment and it seemed like a division which might need to be sold off. However, Samsung is **investing \$22 billion** into its network business and has set a goal of securing **20 percent** of the market by 2020. If Huawei is unable to sell its equipment in many foreign markets, it creates an opportunity for Samsung to compete with Nokia and Ericson to be the dominant 5G network supplier.

But Samsung will face stiff competition for any 5G networking opportunities. Nokia and Ericsson are seen as Huawei's biggest competition for 5G networking equipment and Nokia was **moving to take advantage** of the security concerns about Huawei even before the U.S. ban. In recent weeks its efforts have allowed it to pull even with Huawei in 5G networking contracts.

LG could also benefit from Huawei's difficulties. In recent years, as Huawei's sales have **grown quickly**, LG has seen its shipments of smartphones **continue to decline**. Over the last three years, LG's mobile division has suffered losses of \$2.5 billion. Huawei's ban, and Apple's slow move into 5G phones, could provide **space for LG** to turn around its smartphone division.

The benefits, and costs, for South Korean firms like Samsung, however, may not always be straightforward. It seems unlikely that Samsung would gain 50 percent of Huawei's overseas market and it will potentially lose revenue from lost Huawei sales as well. Huawei is a key purchaser of Samsung display screens and Samsung Display could face **declining profits** from Huawei's difficulties. However, that could be mitigated if Huawei's lost sales outside of China are captured by other Samsung Display customers such as Apple, Oppo, Vivo, and Xiaomi. All of those firms will be competing on some level with Samsung to capture any lost Huawei sales.

If Samsung and South Korea as a whole stand to benefit, there could also be a downside to the Huawei ban.

Some South Korean firms face potential losses. SK Hynix, the world's second largest memory chip maker, supplies the **DRAM memory chips** for Huawei's flagship P30 phone, but unlike Samsung doesn't have the built in advantage of being both a parts supplier and a smartphone producer to mitigate some losses.

This could further suppress earnings at SK Hynix, and potentially even Samsung, at a time when both companies' **operating profits are down** due to continuing declines in the price of DRAM and slowing demand for semiconductors. Exports of semiconductors declined **30 percent** in May, continuing their downward trend.

It's also unclear how the order on Huawei will **affect foreign companies**. Under U.S. law, foreign firms that supplied Huawei would not be able to continue to supply it with parts that **contained licensed U.S. technology**. The British government is in the process of seeking clarification, but the British firm ARM has already cut its ties with Huawei for this reason. Depending on what U.S. technologies South Korean firms have licensed, they may be unable to **fill the gap of U.S. firms** who will no longer be able to supply Huawei.

If the United States does enforce restrictions on foreign firms using licensed U.S. technology, as should be expected, South Korean firms could find themselves under pressure from China as the tech war expands. In response to the U.S. placing Huawei on the Entity List, China is developing an **"unreliable entity list,"** which would allow it to punish firms or individuals that withhold parts from Chinese firms for non-market reasons or harm China's national interest.

It is also unclear how China will define harming its national interest. If that includes aggressively pursuing Huawei's international market share, it could complicate Samsung and other South Korean companies' ability to take advantage of the Huawei ban even if the United States didn't pressure South Korean firms to scale back their business with Huawei.

More critically for South Korean firms like Samsung and SK Hynix, the U.S. decision on Huawei, and last year on ZTE, will likely only hasten Chinese efforts to move forward with Made in China 2025. Huawei already had its own semiconductor arm to supply some of the chips it needs, and the Chinese government has been backing the **development of firms** that could take on Samsung and SK Hynix directly in memory chips, which are the largest export category for South Korea and the primary source of operating profits for Samsung and SK Hynix.

Unless the United States succeeds in developing a long-term **digital wall** around China, South Korea could face Chinese competitors who are no longer dependent upon suppliers from South Korea or other Western countries when the current U.S. restrictions are lifted. If Huawei is able to develop a competing software with Android and source parts from Chinese rather

than foreign suppliers, Samsung could face a more formidable competitor in the future. And other Chinese smartphone producers would likely have similar advantages.

While South Korea is well placed to benefit in the emerging competition between the United States and China over the construction of the world's 5G infrastructure, how it benefits and how lasting those benefits are may be beyond its control. However, what may now seem an opportunity could result in stronger competition for South Korean firms in the long-run.

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